



UNITED STATES RAILROAD RETIREMENT BOARD

OFFICE OF INSPECTOR GENERAL

**Fiscal Year 2001 Financial Statement Audit
Letter to Management
Report No. 02-07, February 8, 2002**

To the Board Members:

We have audited the accompanying consolidated balance sheet of the Railroad Retirement Board (RRB) for the fiscal years ended September 30, 2001 and 2000, and the related: consolidated statements of net cost, changes in net position, budgetary resources, financing and custodial activity (hereinafter referred to as the "principal financial statements") for the years then ended and have issued our report thereon dated February 8, 2002. We conducted our audit in accordance with: generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements."

In planning and performing this audit we considered internal control in order to determine our auditing procedures for the purpose of issuing our report on the RRB's principal financial statements and not to provide assurance on internal control. The maintenance of adequate internal control designed to fulfill the RRB's control objectives is the responsibility of management. Because of inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Also, controls found to be functioning at a point in time may later be found deficient because of the performance of those responsible for applying them. There can be no assurance that controls currently in existence will prove to be adequate in the future as changes take place in the organization.

During our audit of the RRB's principal financial statements, we noted certain matters involving internal control and its operations that we consider to be reportable conditions under standards established by OMB Bulletin 01-02. Reportable conditions are matters coming to our attention that, in our judgment, relate to significant deficiencies in the design or operation of internal control and could adversely affect the RRB's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Our consideration of internal control would not necessarily disclose all matters in internal control that might be reportable conditions.

A material weakness is a reportable condition in which the design or operation of internal control does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to the RRB's financial statements may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

In our report on internal control, dated February 8, 2002, we reported material weaknesses in the RRB's overall control environment and system of information security, and a reportable condition related to debt recovery accounting. During our audit, we also noted other matters involving the RRB's internal control structure and its operation. The details of our findings concerning internal control are presented in the attached summary memorandum. However, neither this letter, nor the attached memorandum, modifies our report on the financial statements dated February 8, 2002, referred to in the first paragraph of this letter.

Our work was not conducted for the primary purpose of making detailed recommendations about the RRB's system of internal control. Had we done so, other matters might have come to our attention that we would have reported to you.

This report is intended solely for the information and use of the management of the RRB, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

We wish to express our appreciation for the many courtesies and cooperation extended to us during the audit.

Very truly yours,

Martin J. Dickman
Inspector General

February 8, 2002

MEMORANDUM ON INTERNAL CONTROL

MATERIAL WEAKNESSESOverall Control Environment

The RRB's overall control environment is not adequate to ensure that agency financial statements will be free of material misstatements and prepared in accordance with applicable guidance. As a result, each financial statement audit since FY 1993 has cited the agency for a material weakness in this area.

We believe that the RRB's present administrative structure is the primary cause of this internal control weakness. Management in the agency's various operating components does not seek assistance across organizational lines to resolve problems related to financial accounting and reporting when they arise. As in prior audits, we continue to observe that the RRB's internal control environment is focused on control objectives and techniques designed to meet the organizational responsibilities of each of the individual operating units, rather than the overall objectives of the RRB. As a result, the agency has experienced difficulties in resolving financial accounting and reporting issues that require cross-organizational cooperation.

Agency management believes that previous reorganizations and the amplified role of the executive committee have eliminated the material weakness. The RRB did not include our finding concerning the overall control environment as a material weakness in the statements of assurance that were issued pursuant to the Federal Managers' Financial Integrity Act, for FYs 1997, 1998, 1999, 2000 or 2001.

The OIG believes the overall control environment continues to be a material weakness. The conditions that led to the original finding continue to exist and have an adverse effect on the agency's ability to meet its internal control objectives related to financial statement reporting. Although the RRB has implemented changes to the agency's organizational structure, we have not observed a related change in the agency's organizational culture.

Information Security

During FY 2001, the OIG conducted a review of information security at the RRB pursuant to the requirements of the Government Information Security Reform Act. Our review disclosed weaknesses in most areas of the RRB's information security program. Significant deficiencies in program management and access controls make the agency's information security program a source of material weakness in internal control over financial reporting.

Access controls cannot be considered fully effective due primarily to inadequacies in password management. Our review identified numerous password management weaknesses in the mainframe, local area and wide area computing environments. The RRB's most notable problem is the agency's inability to police and enforce its recently

adopted policy requiring the use of more complex password configurations. Other weaknesses observed during this review included: passwords that never expire, inactive, duplicate accounts, separated employees and former contractors whose information system privileges had not been revoked.

The overall effectiveness of the RRB's information security program has been undermined by a lack of training among key personnel. Employees with decision-making responsibility for information security have not had adequate formal training in its theory, principles and practice. In addition, the information security program lacks a strong security framework with a central management focal point. These two deficiencies are the underlying cause of many other control problems identified during the audit.

Our report also cites the agency for:

- weaknesses in the security planning and evaluation process;
- inadequacies in the design of controls intended to restrict individual privileges to the minimum required by their employment; and
- a lack of documentation for some security-related activities.

The OIG reported its assessment to agency management in the form of an executive summary dated September 5, 2001. The OIG's detailed findings were published in final form in OIG Audit Report Number 02-04 dated February 2, 2002. In that report, we made specific recommendations for corrective action to strengthen controls in the areas of weakness identified by the audit. In their response, the Bureau of Information Services concurred with most of the OIG's recommendations, and stated that many had already been implemented. However, the agency is still developing target dates for remedial action in some critical areas.

REPORTABLE CONDITION

Accounting for Benefit Overpayment Recoveries

During FY 2000, the OIG identified weaknesses in internal control over debt recovery transactions that adversely impact the ability of the agency to ensure the reliability of financial reporting and the safeguarding of accounts receivable. We identified errors in the recording of debt recovery transactions that included:

- returned benefit payments that had not been credited to debtor accounts;
- benefit payments that had been erroneously credited to debtor accounts as recoveries;
- delayed recording of certain RUIA debt recoveries; and

An examination of these errors identified weaknesses in the related internal controls. The present internal control structure, as it relates to debt recovery accounting, does not:

- consistently provide for the establishment, review and reconciliation of general ledger controlling accounts for benefit payment activity;
- include review of all systems output; and
- prevent or detect certain unauthorized and/or unsupported transactions.

In addition, the present internal control environment does not provide management with sufficient information concerning the number and value of non-conforming transactions to provide the basis for an evaluation of potential financial impact.

These weaknesses in internal control were brought to management's attention in the Office of Inspector General's audit report, #00-16, dated September 29, 2000. Agency management has implemented some of the OIG's recommendations for corrective action. However, they have not taken the recommended action in several key areas, including the implementation of controlling accounts for benefit payments, citing the inability of existing benefit payment sub-systems to support a cost-effective control and reconciliation process.

OTHER MATTERS INVOLVING INTERNAL CONTROL

Problem Resolution Reporting

Logs used to track user reports of mainframe computer problems do not provide management in the Bureau of Information Services (BIS) with an adequate basis for assessing the status or timeliness of problem resolution.

BIS maintains logs that record problems with the RRB's mainframe system as reported by users throughout the agency. Those logs record the problem reported, the date of the report and whether or not the problem has been resolved. However, the log does not identify when the problem was resolved and, as a result, does not provide a basis for assessing the timeliness of problem resolution. In addition, detailed records that support problem resolution are not always consistent with the status reported in the summary log.

We recommend that BIS modify the problem logs to include the date that each reported mainframe computer problem is resolved and develop controls to ensure the consistency of summary and detail records that support the problem resolution process. **(Report Recommendation #00-4)**

Payroll Adjustments

Retroactive payroll adjustments are submitted to BFO on form G-56a. BFO personnel enter the indicated corrections into the Tesseract system, the mainframe application that supports payroll processing. The data entered is not reviewed for accuracy and, as a result, errors may occur and not be detected in time to prevent payment errors.

We recommend that BFO develop a control to ensure the accuracy of retroactive payroll adjustments. **(Report Recommendation #01-1)**

Cost of Living Increase for Grade/Pay Retention Employees

The salaries of certain employees are not mechanically updated for annual cost-of-living increases. These employees have retained a salary commensurate with a higher-paid, previously occupied position than the one they presently hold.

Updated salaries for these employees are manually calculated and entered into the Tesseract system, the mainframe application that supports payroll processing. The data entered is not reviewed for accuracy and, as a result, errors may occur and not be detected in time to prevent payment errors.

We recommend that the Bureau of Human Resources develop a control to ensure the accuracy of manual updates to the Tesseract system. **(Report Recommendation #01-2)**

STATUS OF PRIOR AND CURRENT YEAR RECOMMENDATIONS

We have reviewed the implementation of recommendations resulting from prior audits of the RRB's financial statements. The table below presents a summary of the status of recommendations pending when we issued our "Letter to Management" dated February 8, 2002, in connection with our audit of the RRB's FY 2001 financial statements. The additional recommendations resulting from our audit of the agency's FY 2001 financial statements are also included.

	#	Implemented	In Progress	Declined
BUREAU OF FISCAL OPERATIONS				
Payroll Adjustments	01-1		X	
BUREAU OF HUMAN RESOURCES				
Cost of Living Adjustments	01-2		X	
BUREAU OF INFORMATION SERVICES				
Project Management reporting	00-2	X		
Systems Development Lifecycle	00-3	X		
Problem Resolution Reporting	00-4		X	